

November 30, 1920.

OPINION NO. 951.

TAXATION: INCOME TAX:

Dividends on foreign corporation stock and interest on foreign corporation bonds received by persons or corporations resident or domiciled in Hawaii should be returned as taxable income.

SAME: SAME:

Income received by individuals resident in Hawaii from orchards, farms or other business actually conducted in a foreign jurisdiction is not taxable income.

SAME: SAME:

Income received by an Hawaiian corporation from a business actually conducted in a foreign jurisdiction is not taxable income.

Hon. Delbert E. Metzger,  
Treasurer, Territory of Hawaii,  
Honolulu, T. H.

Dear Sir: I beg to acknowledge the receipt of your communication of the 29th instant, together with a letter from Deputy Tax Assessor Palmer, addressed to you and dated the 27th instant, in which he requests the opinion of this Department upon certain phases of the income tax law of this Territory and wherein he makes the following statement of facts relative to those matters as follows:

1. (a) In checking up the income return made yearly by corporations in this territory I find that a number of them have invested their sinking and reserve funds in mainland and foreign securities such as bonds, stocks and other collateral securities.
2. (b) In the case of individuals I find a number who have invested in oil and mining stocks, also in orchards and farms.
3. (c) In the case of most of our plantation agencies, they have

established offices both on the Pacific coast and in the Eastern states from which they derive a substantial income.

Upon the facts as above set forth he makes the following specific inquiry:

“Is or is not the income from investments such as are named each in class 'a', 'b' and 'c' liable to an income tax under our Hawaiian income tax law?”

So far as I have been able to discover these questions have never been passed upon by the Supreme Court of this Territory nor have they been the subject matter of an opinion from this Department. Their importance is indicated by the fact that the investments in such foreign stock and bonds by one Hawaiian corporation alone, as shown by the list submitted, and the income upon which apparently has not heretofore been taxed, amount to the sum of approximately \$600,000.00, the tax on the income from which would be approximately \$1000.00.

Before discussing in detail the question as to whether income arising from investments in foreign stock, bonds and other securities is taxable income under our statute it should be stated that the mere fact that such investments were made from sinking or reserve funds of corporations does not affect the final answer to that question. It was held by the Supreme Court of the Territory in *Rapid Transit vs. Assessor*, 18 Haw. 15, that money set apart as a sinking fund as permitted by the franchise of the company could not be deducted in computing the net income of the corporation. If the amount set apart as a sinking fund cannot be deducted it is clear that income arising from the investment of those sinking funds cannot be so deducted if it is otherwise taxable.

The inquiry submitted by the deputy tax assessor may therefore be stated as follows:

1. Is the income derived by individuals or corporations resident or domiciled in Hawaii from investments in foreign corporation stocks, bonds and other securities taxable income?
2. Is the income derived by individuals resident to Hawaii from Investments in orchards and farms situate In a foreign jurisdiction taxable income?
3. Is the income derived by Hawaiian corporations from business actually conducted through branch offices situate in a foreign jurisdiction taxable income?

1. Section 1305, R. L. H. 1915, so far as it relates to this precise question, provides as follows:

“There shall be levied, assessed, collected and paid annually from the gains, profits and income over and above \$1500.00 derived by every person residing in the Territory of Hawaii from all property owned—in the Territory—a tax of two per cent on the amount so derived during the taxation period as herein defined.”

This brings us to a consideration of the question as to whether such foreign stocks and bonds are “Property owned in the Territory” within the meaning of the phrase as used in said Section 1305. The great weight of authority sustains the proposition that the situs of stock in a corporation for taxation purposes is the residence or domicile of the owner.

“Since shares of stock in a corporation in the hands of the individual stockholders are personal property, even when the corporation owns land, their situs for purposes of taxation is the residence of the owners or holders within or without the State as the case may be unless there is express statutory provision to the contrary. While a State has no right to tax the property of its citizens when such property is permanently located in another jurisdiction, in the case of the intangible interest of the stockholder there is manifestly no question of physical situs so far as this district property right is concerned and the jurisdiction to tax it is not dependent upon the location of the lands and chattels of the corporation.” 7 Fletcher Cyc. Corporations, 8182.

“The shares of a stockholder is in one aspect something different from the capital stock of the Company; the latter only is the stock of the corporation; the former is the individual interest of the stockholder constituting his right to a proportional part of the dividends when declared and to a proportional part of the effects of a corporation when dissolved after payment of the debts. Regarded in that aspect there is an interest or right which accompanies the person of the owner having no locality independent of his domicile.” *Minot vs. Philadelphia W. & B. R. Co.*, 18 Wall. (U. S.) 206, 21 L. ed. 888.

“Shares of stock are deemed situate at the domicile of the owner for the purposes of taxation.” *Barnell vs. State*, 174 Ind. 143. 90 N. E. 769.

“According to the great weight of authority a tax law subjecting to taxation in general terms all personal property within the State renders shares of stock in a foreign corporation owned by residents of the state liable to taxation.” *Denver vs. Hobb’s Estate*, 58 Colo. 220, 1916 C. Ann. C. 823-831, and cases cited in the case note.

“The ownership of a share of stock so far as the property of the corporation is concerned is but the ownership or right to participate from time to time in the net profits of the business and upon the dissolution of the corporation to a proportion of the assets after the payment of the corporate debts. It is personal property which upon the death of the owner goes to his administrator. Although the entire capital of the corporation may consist of real estate, the owner may sell or dispose of his stock at pleasure, and in so doing works no change or modification in the title to the corporate property. From this it would seem to result necessarily that the situs for purposes of taxation, when not otherwise provided by statute, is that of the domicile of the owner. That shares of stock may be separated from the owner by statute and given a situs of their own was held in *Tappan vs. Merchants Nat’l Bank*, 19 Wall. 490, but when not separated that the situs follows and adheres to the domicile of the owner is supported by the great weight of authority.” *Bradley vs. Bauder*, 36 Ohio St. 28, 38 Ann. Rep. 547.

It is clear from the foregoing authority and many others that might be cited that, for taxation purposes, stock in a foreign corporation is property within the State or Territory where the owner resides or is domiciled.

In a case entitled *Kirtland vs. Hotchkiss*, 100 U.S. 138, 25 Law. ed. 558, the Supreme Court of the United

States announced the same rule with regard to the situs of corporation bonds for taxation purposes and on page 562 of that decision said:

“The creditor (bond holder), it is conceded, is a permanent resident within the jurisdiction of the State imposing the tax. The debt which he holds against the resident of Illinois is property in his hands. 15 Wall., 320. 21 L. ed., 187. It constitutes a portion of his wealth, and from that wealth he is under the very highest obligation, in common with his fellow citizens of the same state, to contribute for the support of the government whose protection he enjoys.

“The debt in question, although a species of intangible property, may, for the purpose of taxation, if not for all purposes, be regarded as situated at the domicile of the creditor. It is none the less property because its amount and maturity are set forth in a bond. That bond, wherever actually held or deposited, is, at best, only evidence of the debt, not the debt itself. The bond may be destroyed, but the debt—the right to demand the repayment of the money loaned, with the stimulated interest—remains. Nor is the locality of the debt, for the purposes of taxation affected by the fact that it is secured by mortgage upon real estate situated in Illinois. The mortgage is but a security for the debt, and, as held by this court in 15 Wall., 323, already cited, the right of the creditor ‘to proceed against the property mortgaged, upon a given contingency, to enforce by its sale the payment of his demand, has no locality independent of the party in whom it resides. It may, undoubtedly, be taxed by the State when held by a resident there.’ Cooley, Tax 15, 63, 134 and 270. the debt in question, then, having its situs at the creditor’s residence and constituting a portion of his estate there, both he and the debt are, for purposes of taxation, within the jurisdiction of the State.”

Section 1307, R L. H. 1915, specifically provides that,

“In estimating the gains, profits and income of any person or corporation there shall be included all income derived from interest upon notes, bonds and other securities except such bonds of the Territory of Hawaii or of the municipalities created by this Territory, the principal and interest of which are by the law of their issuance exempt from all taxation—dividends from the stock of any corporation.”

The only exception to this statutory rule requiring taxation of income arising from bonds and stocks is

that set forth in Section 1308 as amended by Act 157, S. L. 1917, where it is provided,

“That in assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends from the stock of such corporation after the tax of two per centum has been assessed upon the profits of such corporation as required by this chapter.”

I am of the opinion, therefore, and so advise you, that income arising from the dividends on foreign corporation stock and income arising from interest on foreign corporation bonds constitutes taxable income within the meaning of Chapter 94 of the Revised Laws of Hawaii, 1915, as amended.

2. If the investments here referred to be actual investment in orchard and farm lands and not in the stock of a corporation conducting such orchards and farms, then this inquiry must be answered in the negative. Such farm and orchard lands would not be property owned in the Territory within the meaning of Section 1305, nor would the conduct of such orchards and farms constitute the carrying on of a business in Hawaii within the meaning of that section. If, on the other hand, the investment here referred to means an investment in the stock of corporations which are conducting such farms or orchards, the answer would be in the affirmative for the same reasons as set forth in answer to question No. 1.

3. This question is somewhat vague in form and substance. If the branch offices established on the mainland conduct a business of their own independent of the home office, such as the buying and selling of merchandise, the income from such a business would not be taxable for the reason that it is not a business carried on in Hawaii within the meaning of said Sec-

tion 1305. If, on the other hand, such branch offices are established merely for the convenience of the home office for the purpose of assisting in and facilitating the conduct of the business to the home office, I am of the opinion that all income from such branch offices would be taxable income within the meaning of the statute. I am,

Yours very truly,

HARRY IRWIN,

Attorney General.

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